CHAPTER 2. SUPPLEMENTARY LOANS - VALUATION INSTRUCTIONS

2-1. PURPOSES AND KINDS OF SUPPLEMENTARY LOANS. Pursuant to Section 213(j) of the National Housing Act, as amended, supplementary loans for terms of 10, 15, 20, 25, 30, 35 or 40 years (generally not to exceed the remaining term of the original insured mortgage) may be insured for management type cooperatives, for the purpose of financing any of the following:

a. Cost of repairs.

b. Funds to finance the cooperative purchase and resale of memberships.

c. Value of improvements or additional community facilities.

2-2. REQUIREMENTS AND PROCESSING. Since requirements and processing methods differ for each kind of supplementary loan, the three kinds are processed in three different ways. These different procedures are discussed in the following paragraphs.

2-3. LOANS TO FINANCE REPAIRS. In loans to finance repairs, the mortgage will be the lesser of: (a) an amount which, when added to the total unpaid balance of all insured mortgages and other loans on the property, creates a total indebtedness equal to the original principal obligation on the insured mortgage; or (b) the HUD-FHA estimate of the cost of repairs including financing charges; or (c) the actual cost of repairs, including financing charges approved by the Commissioner under cost certification procedures. Valuation processing is as follows:

a. The cost estimate for the repairs prepared by the Cost Analyst will be reviewed and appropriate carrying charges, inspection fee and financing expenses for the work to be done will be added. Title, recording expense and organization expense may not be involved; legal expense should be minimal.

b. The total of the above items is the HUD-FHA estimate of cost of repairs. The amounts may be presented to the Assistant Director Technical Services/Chief Underwriter (ADTS/CU) by memorandum signed by Cost Analyst and appraiser, or in the replacement cost portion of FHA Form 2264.

2-4. FUNDS TO FINANCE COOPERATIVE PURCHASE AND RESALE OF MEMBERSHIPS. Supplementary loans may be insured to finance the cooperative purchase and resale of memberships in an amount which when added to the outstanding balance of the previous mortgage and other loans, does not exceed 97% of the current appraised value of the project for continued use as a cooperative. Valuation processing will be in accordance with instructions for management type cooperatives, existing construction. Loans for this purpose must be processed separately from improvement loans.

2-5. LOANS FOR VALUE OF IMPROVEMENTS OR ADDITIONAL COMMUNITY FACILITIES. For such loans, an increase in the total indebtedness by an amount which does not exceed 97% of the value of improvements or additional facilities is permitted. The outstanding indebtedness thereby created may exceed the original principal obligation of the mortgage if it does not exceed the present project living unit statutory limits.

Eligible improvements may include any appropriate program of rehabilitation or modernization voted by the cooperators and found to be within the ability of the cooperative to assume the added debt service.

2-6. IMPROVEMENT LOANS, VALUATION PROCESSING. Upon request for an examination of the feasibility of the proposed improvements, the appraiser will process in the following steps, using FHA Form 2264-B.:

a. A List of the Proposed Improvements will be obtained and reviewed and the Cost Analyst will enter the cost of the improvements in the space for estimated replacement cost (Section H). To the cost estimate for new improvements the appraiser will add appropriate carrying charges, inspection fee and financing expenses for the work to be done. Title, recording expense and organization expense may not be involved; legal expense should ordinarily be minimal. Neither marketing, land value nor "as is" value is included. Item 80 is amended to read: "Total Estimated Cost of Improvements $_________.

(2-6) b. Current Unit Charges and Annual Budgets for recent years are reviewed and with this information the remaining portions of FHA Form 2264-B (except Sections L and M) are completed to reflect conditions after completion of the improvements and facilities and to show:

(1) New unit charges which will be made by the cooperative, reflecting any changes in debt service, replacement reserves, other common expenses, and operating reserve. The replacement reserve account shall be increased by an annual amount equal to the cost of improvements multiplied by .005.

(2) The estimated new monthly personal benefit expense of the cooperative members.

c. The Total Cost to the Cooperators of both living unit charges and personal benefit expense will be compared with total cost of receiving the same benefits in competitive housing, both on a cooperative basis and on a rental basis. Reproduced copies of sheets from the data bank will be included in the file with items circled in red which indicate costs of receiving similar benefits in competitive housing.

d. The Value to be Found is the worth of the proposes improvements to the cooperative. The appraiser makes the comparisons described in (c) above, employing the Substitution Theory. If the total expense of all charges to the cooperative members, after improvements, is no greater than the total cost of enjoying similar benefits in competitive housing, either cooperative or rental housing, then the value of the improvements will equal the cost of the improvements. The value will not exceed the cost because the substitution theory uses cost as an upper limit of value. If the total expense to the cooperative members, after improvements, is greater than the expense of similar benefits in competitive housing, then the value of the improvements will be less than cost.

e. In the Blank Space Below Item H-80, the following will be typed:

"For Supplementary Loan Purposes, the value of the proposed improvements is $_________."

(2-6) f. Where the Value of the Proposed Improvements is Less Than Cost, the cooperative is not warranted in making the improvements and feasibility is not justified.